

## GENERAL INFORMATION

*The Community Reinvestment Act ("CRA") requires each federal financial supervisory agency to use its authority when examining financial institutions subject to its supervision to assess the institution's record of meeting the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with the safe and sound operation of the institution. Upon conclusion of such examination, the agency must prepare a written evaluation of the institution's record of meeting the credit needs of its community.*

*This document is an evaluation of the CRA performance of Clinton State Bank, Clinton, Minnesota, prepared by the Federal Reserve Bank of Minneapolis, the institution's supervisory agency, as of November 17, 1997. The agency rates the CRA performance of an institution consistent with the provisions set forth in Appendix A to 12 CFR Part 228.*

**INSTITUTION'S CRA RATING:** This institution is rated "Satisfactory."

Several factors support rating the bank's CRA performance satisfactory. First, the bank's lending to borrowers of different income levels and to businesses and farms of various sizes is very strong. Second, the bank maintains a reasonable net loan-to-deposit ratio. Third, the bank has extended a significant percentage of its loans within its assessment area. Finally, the geographic distribution of loans within the assessment area is reasonable.

## **DESCRIPTION OF INSTITUTION**

Based on its size and financial condition, the bank is able to meet the credit needs of its assessment area effectively. The bank received an outstanding rating at its previous CRA evaluation, conducted as of January 2, 1996. The bank operates a full-service office in Clinton. The office is open from 9:00 a.m. to 3:00 p.m. Monday through Thursday and 9:00 a.m. to 5:00 p.m. Friday. The bank's drive-up teller is open from 9:00 a.m. to 3:30 p.m. Monday through Thursday and 9:00 a.m. to 5:00 p.m. Friday. The bank has not opened or closed any offices since the last evaluation.

According to the September 30, 1997, Report of Condition ("ROC"), the bank had total assets of approximately \$44.6 million. Between March 31, 1996, and September 30, 1997, the bank's total assets increased by approximately \$5.7 million, or 14.8%. During that time, the bank's net loans increased by \$5.9 million and deposits increased by \$2.1 million. The bank's loan portfolio is composed of approximately 72% agricultural, 15% commercial, 6% consumer, 6% consumer real estate, and 1% other loans. The composition of the bank's loan portfolio has remained relatively stable since the last evaluation. The bank's loan mix reflects the level of demand for specific types of loans by people, businesses, and farms within the assessment area.

The bank offers a variety of loan products to serve the credit needs of individuals, businesses, and farms within its assessment area. It extends closed-end consumer and residential real estate, and open-end and closed-end agricultural and commercial loans. In addition to these conventional loan products, the bank participates in several federal and state loan programs such as Federal Housing Administration ("FHA") Title I home improvement, Minnesota Housing Finance Agency ("MHFA") home improvement and home energy, Farm Service Agency, Small Business Administration, Minnesota Department of Agriculture Rural Finance Authority, and guaranteed student loans. It also refers potential applicants for secondary-market real estate loans to a mortgage company.

## **DESCRIPTION OF CLINTON STATE BANK'S ASSESSMENT AREA**

The bank has defined its assessment area as Big Stone County, which is located in west-central Minnesota. This area is more specifically defined as block numbering areas ("BNA") 9501, 9502, and 9503.98. BNAs 9501 and 9503.98 are designated as middle-income areas, while BNA 9502 is classified as a moderate-income area. According to 1990 U.S. Census data, the bank's assessment area has a population of 6,285. Ortonville, the county seat, is in BNA 9503.98 and has a population of 2,094. The city of Clinton is in BNA 9501 and has a population of 574. According to information published by the Minnesota Department of Trade and Economic Development, the U.S. Census State Demographer estimated that the 1994 population of the assessment area declined 4.1% to 6,025 since the last census. Other communities in the assessment area include Beardsley, Barry, Graceville, Johnson, Odessa, and Correll, Minnesota.

CRA divides income levels into four categories: low, moderate, middle, and upper. Because the bank's assessment area is not in a metropolitan statistical area, the categorization of a borrower or BNA's income is determined relative to the statewide nonmetropolitan median family income. Low-income individuals have incomes of less than 50% of the statewide nonmetropolitan median family income, while moderate-income individuals have incomes of at least 50% but less than 80% of this amount. The regulation defines a middle-income person as one with an income of at least 80% but less than 120% of the statewide nonmetropolitan median family income. An individual with an income that is 120% or more of the statewide nonmetropolitan median family income is considered an upper-income person. BNAs are classified using similar categories based on the level of median family income in the geography compared

with the 1990 statewide-median family income of \$28,933. The updated 1997 statewide nonmetropolitan median family income is \$38,400. This figure is used to classify borrowers' incomes.

As mentioned previously, two BNAs in the bank's assessment area are classified as middle income and one is classified moderate income. The median family income in BNA 9502 is \$21,214, or 73.3% of the 1990 statewide nonmetropolitan median family income. The median family income in the moderate-income BNA 9502 is not significantly lower than in the two middle-income BNAs. The median family incomes in BNAs 9501 and 9503.98 are \$24,091 and \$25,597, respectively. As a percentage of statewide nonmetropolitan median family income, middle-income BNAs 9501 and 9503.98 are 83.3% and 88.5%, respectively. According to 1990 census data, the assessment area's median household income is \$19,408, while the median family income is \$23,906. Both figures are considerably lower than the Minnesota statewide nonmetropolitan median household and family incomes of \$23,627 and \$28,933, respectively. Of the 2,472 households in the assessment area, approximately 30% are low income, 19% are moderate income, 21% are middle income, and 30% are upper income. Of the 1,727 families in the assessment area, approximately 24% are low income, 24% are moderate income, 25% are middle income, and 27% are upper income. Approximately 16% of the households and 12% of the families have incomes below the poverty level; the percentage of such households and families is higher in the assessment area than in the state's nonmetropolitan areas.

Examiners made a contact with an individual who is familiar with the economic characteristics and credit needs of the assessment area. Information obtained from this individual and bank management was used in evaluating the bank's CRA performance.

The assessment area's major industry is agriculture. Although the local economy depends heavily on agriculture, absentee landowners own increasingly more of the area's agricultural land. The community contact estimated that approximately 60% of the farmland is cash-rented and 55% to 60% of all personal income is from off-farm or nonfarm sources. According to census data, employment trends in Big Stone County mirror the employment trends throughout the nonmetropolitan areas of the state. Farm employment is declining, while government services, nonfarm, construction, and manufacturing employment are increasing. In addition, the need for health-related service businesses is increasing because of the assessment area's aging population.

Bank management and the community contact stated that the assessment area's economy is stable and the unemployment rate is low. One reason for the low unemployment rate is that young people are migrating from the area to avoid accepting the low-salary positions that are available locally. Clinton and several other small towns are becoming bedroom communities. Two employers outside the assessment area that employ local residents are the prison in Appleton, Minnesota, and the Big Stone Cheese Factory in Milbank, South Dakota. The population of the assessment area has declined considerably during the past 10 years; this trend is expected to continue for the next 10 years.

According to 1990 census data, the assessment area has 3,192 housing units. Of these units, 62% are owner occupied, 15% are rentals, and the remaining 23% are vacant. As a percentage of housing units in the assessment area, 63% are in middle-income areas and 37% are in the moderate-income area. Seventy percent of housing units in the middle-income BNAs are owner occupied, while only 49% of housing units in the moderate-income BNA are owner occupied. Bank management and the community contact stated affordable housing is needed to accommodate aging individuals and young, large families. Available housing is between 50 and 80 years old and in need of repair. The housing market is tight because of low demand for new homes and senior citizens remaining in private homes rather than moving to senior housing units or nursing homes.

Bank management and the community contact indicated that area economic development and business organizations are working on a countywide business retention and expansion project. The project's goal is to pool resources from various sources to promote business opportunities. Project participants will first identify immediate needs and retention issues. The participants will focus next on the long-term goal of developing a countywide economic development process.

## **CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA**

The bank's performance in serving the credit needs of its assessment area is satisfactory. Much of the analysis on the following pages is based on a statistical sample of 82 consumer loans, 138 small farm/small business loans, and 42 residential loans originated during the six months preceding the evaluation. The criteria discussed below were reviewed in determining the rating. In assigning an overall rating, the greatest weight was placed on the assessment of lending to borrowers of different income levels and businesses and farms of different sizes and the net loan-to-deposit ratio. These factors most closely measure the bank's efforts to meet the credit needs of its community.

### **LOAN-TO-DEPOSIT RATIO ANALYSIS**

The bank's net loan-to-deposit ratio meets the standards for satisfactory performance. Since the previous evaluation, the bank's quarterly average net loan-to-deposit ratio is 73.1%. According to the September 30, 1997, ROC, the bank's net loan-to-deposit ratio was 81.8%, which is slightly higher than the September 30, 1995, net loan-to-deposit ratio of 79.9%. The following table, based on quarterly ROC data, shows the steady increase of the bank's net loan-to-deposit ratio since the last evaluation.

<b>DATE</b>	<b>DEPOSITS (In thousands)</b>	<b>NET LOANS (In thousands)</b>	<b>NET LOAN-TO- DEPOSIT RATIO</b>
September 30, 1997	\$34,277	\$28,053	81.8%
June 30, 1997	\$34,471	\$26,931	78.1%
March 31, 1997	\$34,675	\$24,234	69.9%
December 31, 1996	\$35,677	\$25,295	70.9%
September 30, 1996	\$34,860	\$25,040	71.8%
June 30, 1996	\$34,277	\$24,134	70.4%
March 31, 1996	\$32,225	\$22,198	68.9%

The fluctuations in loan volume reflect the cyclical nature of an agricultural-based economy. For example, as shown in the table above, net loans typically decrease at the beginning of the year when agricultural borrowers pay down lines of credit as they receive payments for livestock or crops. In addition, the net loan-to-deposit ratio fluctuates with the receipt and level of deposits. The increasing net loan-to-deposit ratio since the last evaluation reflects modest increases in deposits and substantial increases in loans.

According to the June 30, 1997, Uniform Bank Performance Report ("UBPR"), the bank's 78.1% net loan-to-deposit ratio is higher than its national peer group average of 64.4%. The bank's ratio places it in the 82nd percentile compared with its peers. At the last evaluation, the bank's net loan-to-deposit ratio ranked in the 88th percentile compared with its national peers. Management indicated that competition among financial institutions in the assessment area is strong. The following chart shows the asset size and average net loan-to-deposit ratio for the bank and its local competitors.

<b>BANK</b>	<b>TOTAL ASSETS (as of September 30, 1997) (In thousands)</b>	<b>QUARTERLY AVERAGE NET LOAN-TO- DEPOSIT RATIO</b>
Clinton State Bank Clinton, Minnesota	\$44,575	73.1%
Minnwest Bank Ortonville Ortonville, Minnesota	\$49,684	72.3%
Security State Bank of Beardsley Beardsley, Minnesota	\$13,169	73.9%
State Bank of Wheaton Wheaton, Minnesota	\$59,029	57.7%

As shown above, the bank's quarterly average net loan-to-deposit ratio is comparable to the ratios of two of its competitors and significantly higher than the ratio of one competitor. Bank management predicted that as the community's population ages, loan demand will decrease. Information received from the community contact did not identify any unmet credit needs. Furthermore, the June 30, 1997, UBPR indicates the bank's average net loans to assets was 61.7%. The average for all banks in Minnesota with assets between \$25 million and \$100 million is 63.1%. Accordingly, the bank devotes a similar percentage of its assets to net loans as comparable-sized institutions in Minnesota.

The bank's net loan-to-deposit ratio is reasonable. The analysis revealed that the bank's ratio is high and increasing, is comparable to the local competitors' ratios, and is higher than the national peer group's average ratio. Further, the evaluation did not reveal any unmet credit needs. For these reasons, the bank's net loan-to-deposit ratio meets the standards for satisfactory performance.

#### COMPARISON OF CREDIT EXTENDED INSIDE AND OUTSIDE THE ASSESSMENT AREA

The bank's lending activity in the assessment area exceeds the standards for satisfactory performance. A review of the statistical sample of loans originated by the bank during the past six months reveals that the bank extended a significant majority of its loans inside the assessment area. The following table shows the percentage of loans inside and outside the assessment area based on total number and loan amount in each major loan category.

<b>DISTRIBUTION OF LOANS INSIDE AND OUTSIDE OF THE ASSESSMENT AREA</b>								
<b>Loan Type</b>	<b>Inside Assessment Area</b>				<b>Outside Assessment Area</b>			
	Number of Loans	%	Amount of Loans (In thousands)	%	Number of Loans	%	Amount of Loans (In thousands)	%
Consumer	70	85	\$ 325	83	12	15	\$ 69	17
Residential Real Estate	39	93	\$ 858	90	3	7	\$100	10
Small Farm/ Small Business	122	88	\$1,400	86	16	12	\$235	14
Total	231	88	\$2,583	86	31	12	\$404	14

Since the last evaluation, the bank's lending activity in the assessment area has remained relatively stable. The relative proportion of small farm/small business loans extended to borrowers in the assessment area did not change since the last evaluation. However, the relative proportion of consumer loans that the bank extended to borrowers in the assessment area increased. Conversely, the bank's residential real estate loan activity in the assessment area declined slightly. The last evaluation revealed that the bank

extended 79% of its consumer loans, 97% of its residential real estate loans, and 88% of its small farm/small business loans in its assessment area.

As illustrated above, the bank makes a substantial majority of its loans to people, businesses, and farms in its assessment area. Based on the high concentration of loans originated within the assessment area, the bank exceeds the standards for satisfactory performance in this category.

#### LENDING TO BORROWERS OF DIFFERENT INCOME LEVELS AND TO BUSINESSES OF DIFFERENT SIZES

The bank's level of lending to individuals of different income levels and to businesses and farms of different sizes significantly exceeds the standards for satisfactory performance. As previously mentioned, CRA groups income levels into four categories: low, moderate, middle, and upper. The following table shows the percentage of consumer and residential real estate loans made to borrowers of different income levels.

<b>DISTRIBUTION OF LOANS IN THE ASSESSMENT AREA BY BORROWER INCOME LEVEL*</b>				
<b>Loan Type</b>	<b>Low-Income Borrowers</b>	<b>Moderate-Income Borrowers</b>	<b>Middle-Income Borrowers</b>	<b>Upper-Income Borrowers</b>
<u>Consumer</u>				
Total Number of Loans	44%	36%	11%	9%
Total Amount of Loans	26%	32%	13%	29%
<u>Residential Loans</u>				
Total Number of Loans	23%	26%	28%	23%
Total Amount of Loans	27%	13%	41%	19%
*Income level based on Minnesota's 1997 nonmetropolitan median family income of \$38,400.				

The data in the table indicate that the bank originated a significant majority, 80%, of its consumer loans to low- and moderate-income borrowers. In addition, 58% of the total amount of the bank's consumer loans were made to low- and moderate-income borrowers. Since low- and moderate-income people typically qualify for smaller consumer loans than middle- and upper-income people, the fact that the bank extended relatively less of the total dollar amount of consumer loans to low- and moderate-income people is not unreasonable. The bank's residential real estate lending to low- and moderate-income borrowers comprises 49% of the number and 40% of the dollar amount of its total real estate loans.

As previously mentioned in the Description of Assessment Area section, approximately 49% of the households and 48% of the families in the bank's assessment area are classified as low and moderate income based on the 1990 census figures. With respect to consumer loans, the bank's lending to low- and moderate-income borrowers is significantly higher than expected given the assessment area's demographics. Although its real estate lending to low-income borrowers is less than expected, the bank has extended more residential real estate loans than expected to moderate-income borrowers given the assessment area's demographics. Since the last evaluation, the bank's residential real estate lending to low- and moderate-income borrowers has increased. The last evaluation revealed that the bank extended 5% of its residential real estate loans to low-income borrowers and 12% to moderate-income borrowers.

As previously mentioned, the bank participates in several government loan programs to serve the needs of low- and moderate-income borrowers. The bank is an active participant in the MHFA and FHA Title 1 home improvement loan programs. These loan programs are directed toward low- and moderate-income individuals. The bank is commended for being an active lender to the low- and moderate-income residents of its assessment area.

As previously mentioned, approximately 87% of the bank's loan portfolio is agricultural and commercial loans. Small farm loans are defined as loans with original principal amounts of \$500,000 or less, and small business loans are loans with original principal amounts of \$1 million or less. All of the 122 small business and small farm loans in the bank's assessment area were to borrowers with gross annual revenues of \$1 million or less. In addition, all of these loans were for amounts less than or equal to \$100,000. The bank's lending patterns reflect the characteristics of the small business and small farm lending markets of west-central Minnesota.

Based on the bank's high level of consumer and residential real estate lending to low- and moderate-income individuals, its participation in residential real estate loan programs, and the level of small business/small farm lending, the bank exceeds this category's standards for satisfactory performance.

#### GEOGRAPHIC DISTRIBUTION OF LOANS

The distribution of the bank's loans throughout the assessment area is reasonable and meets this category's standards for satisfactory performance. As previously discussed, the bank's assessment area includes two middle-income BNAs and one moderate-income BNA. As discussed in the Description of the Assessment Area, as a percentage of statewide nonmetropolitan median family income, the middle-income BNAs' median family incomes are 83.3% and 88.5% while the moderate-income BNA's median family income is 73.3%. There are no low- or upper-income BNAs in the assessment area. Bank management indicated the low-, moderate-, middle-, and upper-income residents are not concentrated in any particular area but are dispersed throughout the assessment area. The following table illustrates the distribution of loans by BNA income level.

<b>DISTRIBUTION OF LOANS IN THE ASSESSMENT AREA BY BNA INCOME LEVEL</b>		
<b>Loan Type</b>	<b>Moderate-Income BNA</b>	<b>Middle-Income BNAs</b>
<u>Consumer</u>		
Total Number of Loans	16%	84%
Total Amount of Loans	23%	77%
<u>Residential</u>		
Total Number of Loans	18%	82%
Total Amount of Loans	17%	83%
<u>Small Farm/Small Business</u>		
Total Number of Loans	28%	72%
Total Amount of Loans	30%	70%

A tract-by-tract analysis reveals that the bank's loans are reasonably distributed throughout the moderate- and middle-income BNAs. The distribution of consumer, residential real estate, and small farm/small business loans indicates that a significant majority of loans were made in the middle-income BNAs. The high percentage of loans originated in the middle-income BNAs is reasonable given the bank's location in

BNA 9501 and because approximately 69% of the assessment area's population resides in the middle-income BNAs.

The concentration of residential real estate loans in the middle-income BNAs is also reasonable. Although the bank's residential real estate lending in the middle-income BNAs is higher than the concentration of people (69%) and housing units (63%) in these areas, several factors affect the bank's lending activity in the moderate-income BNA. As previously mentioned, 71% of housing units in the middle-income BNAs are owner occupied while only 49% of housing units in the moderate-income BNA are owner occupied. The moderate-income BNA contains only 28.9% of the owner-occupied units in the assessment area. In the assessment area, there is low demand for new housing and limited housing availability. Finally, the bank faces strong competition from several financial institutions located in the moderate-income BNA.

Although concentrated in the assessment area's middle-income BNAs, the bank's lending activity is reasonable. The local demographic characteristics, demand for residential real estate loans, and competition among financial institutions affect the bank's ability to extend loans to borrowers in the moderate-income BNA. Since consumer and residential real estate loans comprise 12% of the bank's loan portfolio, the geographic distribution of these loans appears reasonable. Therefore, based on the tract-by-tract analysis as well as the bank's opportunity to extend loans in the moderate-income area, the bank meets the standards for satisfactory performance in this category.

#### GENERAL

The evaluation did not reveal any substantive violations of fair lending laws or regulations. The evaluation revealed an isolated violation of a technical aspect of Regulation B--Equal Credit Opportunity Act. Bank management promised prompt corrective action. In addition, the bank has not received any CRA-related complaints since the last evaluation.



## **PUBLIC DISCLOSURE**

November 17, 1997

Date of Evaluation

## **COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION**

Clinton State Bank

Name of Depository Institution

092712000000

Identification Number of Institution

Clinton, Minnesota

Address of Institution

Federal Reserve Bank of Minneapolis  
90 Hennepin Avenue, P.O. Box 291  
Minneapolis, Minnesota 55480-0291

NOTE: This evaluation is not, nor should it be construed as, an assessment of the financial condition of this institution. The rating assigned to this institution does not represent an analysis, conclusion, or opinion of the federal financial supervisory agency concerning the safety and soundness of this financial institution.